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2008 ANNUAL REPORT OF BELGIUM TO THE EUROPEAN COMMISSION

SUMMARY AND MAIN DEVELOPMENTS

2. Summary/main developments during the year under review

2.1. Organisational structures and powers of the Belgian regulatory authorities

In Belgium, the Federal State and the regions share the competence relating to the electricity and natural gas market. The distribution of areas of competence was not changed in 2007.

2.1.1. The Commission for Electricity and Gas Regulation (CREG)

Composition

The CREG is composed of two bodies: the Management Board and the General Council.

a) Management Board

The restructuring of the CREG pursuant to the Law of 20 July 2006 comprising various provisions¹ entered into force on 31 December 2006. The Management Board henceforth consists of a chairman, who is responsible for the management of the CREG, and three directors, who are in charge of the directorate for price (gas and electricity), the directorate for technical operation (gas and electricity) and the administrative directorate respectively.

The members of the Management Board (1 chairman and 3 directors) are appointed by royal decree discussed in the Council of Ministers for a renewable term of six years. They are chosen for their competence and are subject to certain rules regarding incompatibilities with their office and conflicts of interest.

On this basis, the chairman and the three directors have concluded an agreement sui generis with the Minister for Energy for their term of office. This agreement expires as of right at the end of said term of office or upon the appointment of a chairman/director by royal decree.

Either party may moreover terminate the agreement immediately and unilaterally when exceptional

¹ Moniteur belge [Belgian Official Gazette] of 28 July 2006.

circumstances render the performance thereof definitively impossible, or when the other party commits serious breach of its duties and obligations. Apart from such circumstances, a chairman/director may terminate the agreement by service of 12 months' notice.

b) General Council

The areas of competence of the General Council were fundamentally altered in 2007. The Council no longer has the authority to assess the way in which the Management Board carries out its tasks. Administrative supervision of the CREG has been transferred to the Council of Ministers (cf. point on independence infra). The composition of the General Council was not altered in 2007. The appointment and resignation of members of the General Council are regulated by ministerial decree.

Main statutory objectives

The CREG is the federal regulator for Belgium.

On the basis of the Law of 29 April 1999 on the organisation of the electricity market (Electricity Act) and the Law of 12 April 1965 on the transmission of gaseous and other substances by pipelines (Gas Act), the CREG is entrusted with an advisory task on behalf of the government regarding the organisation and functioning of the electricity and natural gas markets on the one hand, and a general task of supervision and monitoring of the application of the relevant laws and regulations on the other.

As announced in the previous report, a law altering the tasks entrusted to the CREG was adopted in 2005. These changes entered in force in large measure in the beginning of 2006. This new law does away with the obligation to cooperate with the competition authority. It transfers the competence for defining the methodology relating to the fair profit margin (assessment of regulated assets and the cost of capital) regarding the grid tariffs from the CREG to the Federal Government. It moreover stipulates that the CREG shall henceforth give an opinion on the indicative programme of the electric power generation units and natural gas supply. Previously, the CREG had a competence for proposal, and not for advice, on such matters.

Furthermore, at the time of the drafting of this report, the Law of 8 June 2008 comprising various provisions was adopted. This new law provides, under chapter IX Energy, for the strengthening of the powers and rights of the federal regulator, by entrusting the CREG in particular with the supervision of transparency and competition on the electricity and natural gas markets, the control

of prices on these markets, the essential interests of consumers, and the proper fulfilment of the public service obligations by the companies concerned.

These aspects will be broached in greater detail in the report on the year 2008.

Reporting and independence

Pursuant to the relevant legislative provision in force, the CREG must, by 1 May of each year, submit to the Minister for Energy, a report on the performance of its tasks, on the state of operating expenses and the way they were covered, and on developments on the electricity and natural gas markets. The Minister for Energy then forwards this annual report to the federal legislative chambers and to the regional governments.

Pursuant to the amendments to the Electricity Act adopted in July 2006, the Management Board of the CREG has moreover been required, as of 30 January 2007², to submit to the Minister for Energy, by 30 October of each year, a policy plan along with the draft budget of the CREG for the subsequent year.

This policy plan must contain the strategic objectives intended to implement the general political policy of the government as well as the specific rules and conditions according to which missions, assigned by the legislator to the regulator, will be accomplished.

A comparison can thus be drawn by the Minister for Energy between the general policy objectives on the one hand, and the progress in achieving them as provided in the CREG's annual report on activities on the other. The federal government will evaluate the achievement of objectives of said policy plan, and may give instructions for implementation or concrete policy guidelines to the Management Board of the CREG.

Motivation and publication of the acts of the CREG

The acts of the CREG must be formally motivated, unless otherwise stated. The motivation consists of indicating, in the act, de facto and de jure considerations underpinning the decision, which must be adequate.

The definitive versions of the acts of the CREG are public and published on its website, unless decided otherwise by the CREG bodies that took the decision. The CREG must nonetheless take

² After the entry into force, on 30 January 2007, of Article 135 of the Law of 20 July 2006 comprising various provisions.

account of the confidential nature of data transmitted to it, where applicable.³

Cooperation with other national authorities

The legislation does not provide (any longer)⁴, in 2007, for formal cooperation with other national authorities. The CREG nonetheless maintains regular contacts with the Energy administration, and meets with the three regional energy regulators (BRUGEL, CWaPE and VREG) on a monthly basis to broach topical issues concerning the natural gas and electricity markets.

Nevertheless, the afore-cited Law of 8 June 2008 comprising various provisions, reintroduces formal cooperation between the CREG and the Competition Council. The CREG must in fact henceforth (i.e. as of June 2008) report to the Council any presumed violations by electricity and natural gas companies (unfair trading practices, anti-competitive behaviour, prices not objectively justified in comparison with the company's costs), submit a copy of the report it has sent the Minister containing its observations, and provide such confidential information as necessary.

Appeal against the decisions of the CREG

On 1 February 2006, a new procedure of appeal against the decisions of the CREG entered into force. In principle, said decisions may henceforth be contested by means of summary proceedings before (i) the civil courts (Brussels court of appeal) or (ii) the Competition Council. Furthermore, the tariff decisions of the CREG may be suspended by (iii) the Council of Ministers.

(i) Appeals to the Brussels court of appeal must be lodged within 30 days as of the notification/publication/communication of the decision.

Within 3 working days of being lodged, the appeal is notified by the clerk of the court to all the parties joined by the appellant to the proceedings. Within the same 3-day period, the clerk of the court asks the Management Board of the CREG to send the administrative file relating to the impugned action. Said file must be submitted within 5 working days as of receipt of the request.

The court of appeal fixes the time limits within which the parties can submit their written observations. It also fixes the date of the hearing.

³ CREG Communication of 6 July 2006 on the communication of decisions, proposals, opinions and studies (available at www.creg.be).

⁴ In 2005, a Law altering the tasks of the CREG did away with the requirement to cooperate with the competition authority (cf. *supra* in the text).

The court decides within 60 days as of the lodging of the appeal. It is called upon to rule on the merits of the case and has full jurisdiction.

Decisions of the CREG likely to be impugned before the Brussels court of appeal pertain:

- For gas: to the approval of the conditions of access to the transmission systems and the verification of the application of said conditions, the fulfilment of public service obligations, the bookkeeping of companies in the sector, the tariffs and the administrative fines;
- For electricity: to the verification of compliance by the transmission system operator with the corporate governance and unbundling rules, the application of the grid code and development plan, the fulfilment of public service obligations, the calculation method and the calculation of costs and losses, the tariffs, the bookkeeping of companies in the sector, the tariffs and the administrative fines.

In practice, up to 2007, appeals from the decisions were all but systematically introduced against the tariff decisions of the CREG, and have led to a series of rulings by the Brussels court of appeal. These rulings have had an impact on the tariffs at different levels:

First, a major change occurred in the method used to establish the bonus / malus. More specifically, in previous operating years, the CREG distinguished between the differences between the budgeted figure and the actual figures from cost control (or the lack of cost control), which were qualified as bonus (malus) on the one hand, and those inherent to budgeting (budgeting errors, failure to achieve budgeted projects, differences in the volumes estimated, etc.), qualified as operating result, on the other. In its decisions of 27 February 2007, the Brussels court of appeal ruled that the distinction drawn by CREG between the operating result and a bonus (malus) cannot be sustained. The court moreover ruled that this bonus / malus had to be established by the difference between the actual result produced by the application of the tariffs approved by the CREG and the budgeted result (fair profit margin) covered by these tariffs, thereby prohibiting an ex-post recalculation of the fair profit margin on the basis of the actual development of the invested capital, as CREG had done in previous operating years.

The CREG has complied with the ruling and consequently has applied these principles to determine the bonus / malus resulting from the application of the tariffs. The CREG nonetheless believes that this method does away with any inducement to reduce costs on the part of distribution system operators who, on the contrary, are encouraged to overestimate their budgeted

tariffs and in particular the budgeted profit margin. Furthermore, the definition of bonus / malus upheld by the court of appeal reduces significantly the power to assess the reasonable nature of costs when examining annual reports.

The Brussels court of appeal also proved very severe in respect of certain discretionary powers of the CREG. The CREG even fears that it will no longer be able to fulfil its legal tasks properly.

For instance, according to the court, the CREG does not have any regulatory competence as regards determining depreciation rules; its authority to determine the profit margin is limited; it has to accept bookkeeping as the cornerstone of tariff setting; it only has limited powers to assess the reasonable nature of costs; and as regards the distribution of gas, it is no longer allowed to assess the reasonable nature of costs imposed by another competent authority. For all these reasons, the court of appeal in Brussels has decided to annul the contested decisions.

Consequently, in 2007, the CREG had to review the decisions for four distribution network operators relating to the 2006 operating year. To actually implement these corrections, the CREG decided not to recalculate the tariffs for the 2006 operating year, which would involve adjusting invoices for 2006, but to impute the corrections resulting from the judgements to the tariffs for 2008.

These judgements will inevitably lead to higher tariffs as of 2008.

In order to safeguard the cost reductions achieved during the period from 2003 to 2006, the CREG has also adopted a proactive attitude and in cooperation with the distribution system operators has sought a solution to put an end by mutual agreement to the appeals lodged against its decisions. It succeeded in reaching a settlement out of court with the distribution network operators in the mixed sector, which put an end to all disputes with the latter.

(ii) Appeals to the Competition Council must be lodged within 30 days as of the notification/publication/communication of the decision.

The appeal is subject to the rules of investigation and procedure relating to restrictive competitive practices laid down by the Laws of 10 June 2006 “on the protection of economic competition” and “establishing the Competition Council.”

The Council decides within four months as of the lodging of the appeal.

Decisions of the CREG likely to be contested before the Competition Council pertain:

- For gas: to the approval or rejection of the transmission system operator's decision relating to access to the transmission grid, and methods for allocating the quantity of gas available at interconnection points with foreign transmission grids.
- For electricity: to the application of the grid code (only when the decision concerns the approval, the request for review of refusal of approval), the approval or rejection of the transmission grid operator's decisions relating to access to the transmission grid, the methods for allocation of interconnection capacity for electricity exchanges with foreign transmission grids.

(iii) The CREG must notify the Council of Ministers of the tariff decisions it has taken immediately after they have been adopted. Within 30 days of the receipt thereof, the Council of Ministers may, on proposal of the Minister for Energy, by motivated decision, suspend the enforcement of the tariff decisions by which CREG violates the law or harms the general interest, or the decisions that the Council of Ministers considers to be contrary to the guidelines of the country's energy policy, including the government's objectives for the country's energy supply. The CREG has then 15 days as of the suspension to change the suspended decision by complying with the motivated decision of the Council of Ministers.

2.1.2. “De Vlaamse Reguleringsinstantie voor de Elektriciteits- en Gasmarkt (VREG)” [The Flemish Regulatory Authority for the Gas and Electricity Market]

The VREG is the regional regulator for Flanders.

The mission and functioning of the VREG are governed by the Decree of 30 April 2004 on the creation of an external autonomous agency of public law, the “Vlaamse Reguleringsinstantie voor de Elektriciteits- en Gasmarkt” (Flemish Regulatory Authority for the Gas and Electricity Market). This decree is in line with a project to reform the Flemish public administration.

On 1 April 2006, the tasks and functioning of the VREG were altered on several points after the entry into force of this decree:

- As of 1 April 2006, the daily management of the VREG is entrusted to a managing director and not the executive committee composed of the chairman and managers;
- As of 1 April 2006, the VREG has a board of directors composed of three directors. This board of directors replaces the control by the government commissioner;
- The VREG has been expressly entrusted with an information task regarding the functioning

of the energy market as well as the prices and conditions offered by the suppliers.

The board of directors of the VREG is appointed by the Flemish Government and the managing director is a member of said board.

The VREG has the power to impose fines, issue supply licences and appoint the distribution system operators.

The VREG reports to the Flemish Government and its decisions can be appealed to the Council of State.

Finally, the VREG participates in informal consultations with the other Belgian energy regulators, in investigations by the Competition Council and in the activities of the Directorate General for Control and Mediation of the FPS⁵ Economy.

2.1.3. “La Commission wallonne pour l’Energie” (CWaPE) [Walloon Energy Commission]

The CWaPE is vested with a mission to provide advice to the public authorities on the organisation and functioning of the regional gas and electricity markets on the one part, and a general mission to supervise and monitor the application of laws and decrees relating thereto on the other (Decree of 12 April 2001 on the organisation of the electricity market and of 19 December 2002 on the organisation of the gas market).

Its objectives, composition, powers and the legal provisions defining its missions in general (Decree of 12 April 2001 on the organisation of the electricity market and of 19 December 2002 on the organisation of the gas market) were not altered in 2007.

It is worth noting, however, that amendments to the Decrees of 12 April 2001 and of 19 December 2002 will enter force in 2008. The bill proposes an in-depth reorganisation of the structure of the CWaPE. At present, the decree provides that it is composed of a chairman and directors, without specifying the nature of the relations between the chairman and directors. The bill reorganises the CWaPE in a hierarchical structure, headed by the chairman. The directors, each in charge of a directorate, report directly to the chairman. The new bill also charges the government with the task to define the status of the chairman and of the directors, as well as the procedures for their appointment. The directorates are redefined in accordance with the different expertise required of

⁵ Federal Public Service.

the directors.

The bill moreover provides for an increase in the investigative powers of the CWaPE in performing its tasks. It also strengthens the powers of the government concerning the supervision exercised over the CWaPE (power of positive injunction).

The current Electricity Decree established a conciliation and arbitration service in the CWaPE, as well as an independent body called the “Chambre d’Appel (“Appeal Board”) in charge of settling disputes about access to the grid and the application of technical regulations. Only one case has been referred to the Conciliation and Arbitration Service in six years of operation. No case at all has been referred to the Appeal Board. The bills are intended to rationalise and simplify procedures in this regard.

By virtue of new provisions, a regional ombudsman service is to be created in the CWaPE. Furthermore, any and all disputes relating to access to the grid and the application of the Technical Regulation could be brought before a subsidiary body of the CWaPE, the “Chambre des litiges” (“Litigation Board”), composed of the chairman and directors of the CWaPE. Decisions of the Litigation Board would be subject to appeal.

As all these changes have not yet entered into force, we shall broach them in greater detail in the report on the year 2008.

2.1.4. La Commission de régulation pour l’énergie en Région de Bruxelles-Capitale” (BRUGEL) [Energy Regulatory Commission in the Brussels-Capital Region]

On 14 December 2006, the Government of the Brussels-Capital Region, enacted an ordinance⁶ establishing a new regulatory authority for the Brussels-Capital Region: the “Commission de Régulation pour le gaz et l’électricité en Région de Bruxelles-Capitale” (BRUGEL) [Energy Regulatory Commission in the Brussels-Capital Region].

This Commission, which was established in concrete form by the appointment of the members of the Board of Directors by the Government of the Brussels-Capital Region on 25 September 2007, has been entrusted with the tasks to:

⁶ 14 December 2006 – Ordinance amending the ordinances of 19 July 2001 and of 1 April 2004 on the organization of the gas and electricity market in the Brussels-Capital Region and repealing the ordinance of 11 July 1991 on the right to minimum electricity supply and the ordinance of 11 march 1999 establishing measures to prevent the cutting off of gas supply for household use.

- 1° provide opinions, studies or reasoned decisions and to submit proposals;
- 2° carry out, at its own initiative or at the request of the competent Minister or the Government, research and studies relating to the gas and electricity market;
- 3° publish a yearly report on the results of the supervision on the annual operating output of quality co-generation installations;
- 4° make proposals to the Government to amend the technical regulations, and supervise their application;
- 5° establish the conditions for authorisations issued for the construction of new direct lines;
- 6° receive and process complaints about public service obligations;
- 7° approve, each year, the report on the functioning of the market of green certificates and guarantees of origin drawn up for the Government;
- 8° cooperate with the regional, federal and European regulators of the gas and electricity markets;
- 9° submit each year a report to the Government of the Brussels-Capital Region on the fulfilment of its obligations, the development of the regional gas and electricity market and the fulfilment of the public service obligations by the distribution system operator and the suppliers, especially on the rights of residential consumers;
- 10° carry out all other tasks entrusted to it by ordinances and decrees, regulations and decisions of the Government of the Brussels-Capital Region on the organisation of the gas and electricity market;
- 11° dispose of in situ inspection powers and carry out such inspections;
- 12° publish its opinions, studies and decisions within 21 days, except as regards elements for which confidentiality is required;
- 13° place at the disposal of customers tools for information on the situation of the electricity market as well as on the present ordinance, based in particular on information requested periodically from suppliers and distribution system operators.

BRUGEL is composed of a chairman and 4 directors appointed by the Government for a renewable term of 5 years. In the event of serious breach of his duties, a member of the board of directors may, on the proposal of the Commission, be dismissed by the Government. The Commission shall be supervised by the Government through two Government commissioners appointed and dismissed by the Government. The Government commissioners may appeal any decision that they deem contrary to the ordinance, the implementing decrees of the ordinance or the general interest. The appeal is suspensive. The commissioners appeal to the Government. If the Government has not decided within fifteen working days as of the date of suspension, the decision is final. The Government notifies the annulment of the decision to the Commission.

2.2. Main developments in the gas and electricity markets

2.2.1. Wholesale market

2.2.1.1. Market integration

a) Electricity

- *Participation of the CREG in the pentilateral energy forum*

The CREG participated actively in the pentilateral energy forum set up in 2007, which brings together the governments, regulators, transmission grid operators and power exchanges of the Centre-West region of Europe⁷. The meetings held under this forum lead to the signing of a memorandum of understanding with a view to introducing flow based market coupling, on the one hand and improving the conditions relating to security of supply.

- *Initiatives taken by the regulators concerning the regional integration of electricity markets*

In February 2007, the regulators of the Central-West European Region published their action plan for the 2007- 2009 period⁸, with the aim of accelerating the regional integration of electricity markets. This plan makes a list of various priority areas requiring intervention and identifies specific actions with an appropriate implementation schedule. These priority areas are the harmonisation and improvement of explicit auctioning mechanisms, the creation of flow-based market coupling, the introduction of cross-border intraday and balancing trade, drawing up a common method to calculate interconnection capacities, maximising interconnection capacities, working out a regional investment plan for the transmission grid, transparency and regional market supervision.

In this same context and so as to enable the application of new guidelines on congestion management (Annex to Regulation (EC) n° 1228/2003 on conditions for access to the network for cross-border exchanges in electricity) in the Central-West Europe region, the regulators concerned published their report describing the procedure for the implementation of the transparency aspect of these guidelines.⁹ This report was preceded by an in-depth consultation of the market players.

⁷ Belgium, the Netherlands, Luxemburg, France and Germany.

⁸ Available at <http://www.creg.be>

⁹ Available at <http://www.creg.be>

The role of the ERGEG and the regional initiatives remains very important for promoting market integration. It is important to note, nonetheless, that sizeable market power subsists on all the markets, and in particular on the generation and adjustment markets. For there is no integration of adjustment markets.

- *Coupling of the Belgian, Dutch and French markets*

The D-1 DAM (*Day Ahead Markets*) of Belgium (Belpex), the Netherlands (APX) and France (Powernext) were successfully matched in 2007. The three markets only seldom operated in isolation from one another, i.e. 1.75%. Belpex and Powernext had the same prices listed 88% of the time, and Belpex and APX 73% of the time. In 2007, the prices on the three markets were therefore on average fairly close to one another and relatively low, with an average annual price of €41/MWh.

Congestion rents were nonetheless observed during the attribution of the daily capacity on the interconnections. In 2007, the total congestions rents amounted to €43 million. These rents were very volatile in 2007, with very high values recorded on certain days.

The improved integration of the markets, following the coupling of the Belgian, French and Dutch markets, did not result in an increase of net imports for Belgium, however. In fact, net physical imports of electricity amounted to approximately 6.6 TWh in 2007¹⁰, a fall of around 3.4 TWh compared with 2006. This brings the net physical imports more or less back to the 2005 level (6.2 TWh). Gross physical imports in 2007 amounted to approximately 15.7 TWh, compared with 18.7 TWh in 2006. Gross physical exports stood at 9.0 TWh, compared with 8.6 TWh in 2006.

b) Natural gas

- *Initiatives taken by the regulators concerning the regional integration of natural gas markets*

As regards the regional integration of the natural gas markets, the three gas regions, set up by ERGEG, continued their activities, under the aegis of the regulators, by removing barriers to trade and competition with a view to speeding up the regional integration of the gas markets.

Against this background, in October 2007, the regulators of the natural gas markets of the

¹⁰ Source: ELIA – provisional data, January 2008.

European North/Northwest region, sealed their intensive cooperation by signing a Memorandum of Understanding which, in spite of the fact that it is not legally binding, should help ensure that the decisions and processes of the regulators concerned are more efficient, more consistent and more coordinated. In 2007, the emphasis was on issues such as transparency, balancing rules, the accessibility of the hubs and cross-border capacity, while for the CREG, the priority was the coordination, in conjunction with the French regulator, of the double open season process and the harmonisation of transmission services around the French-Belgian interconnection point at Taisnières/Blaregnies. This harmonisation has led to a doubling of the number of suppliers active at this entry point for the French market, and a short-term reservation rate of 100% for the entry capacity available on the French market.

- *Interaction between the Belgian market and the natural gas transit market: proceedings against the CREG*

At national level, although required by the second gas directive, 2003/55/CE, the continuation of the integration of the Belgian market and the gas transit market has been constantly delayed, by all means, by the parties belonging to the incumbent's group. It is worth pointing out in particular the different appeals lodged by Fluxys, Distrigaz and Distrigaz&C° against the CREG decision to serve formal notice on Fluxys and Distrigaz&C° to hand over the transit activities from Distrigaz&C° to Fluxys on the one hand and against the CREG study on determining the value of this transfer on the other.¹¹ It was not until 30 June 2008, that the two protagonists issued a joint press release announcing the approval by their respective boards of directors of the proposed takeover of Distrigaz&C° by Fluxys.

- *Liquidity on the wholesale market*

The overall situation on the natural gas wholesale market, i.e. the market for supply to customers directly connected to the Fluxys grid and the city-gates, scarcely changed in 2007.

The wholesale market in Belgium has actually remained highly concentrated and characterised by a very limited number of actors with an important market share. Thus, only three supply companies held a market share of more than 5% and together accounted for an aggregated market share of 99.4%.

The incumbent operator on this market managed to retain its dominant position in 2007, even if its

¹¹ Cf. CREG, Annual Report 2007, point 2.6.3.2.

market share continued to fall during that year: this share amounted to 78.2% in 2007, or a fall of -2.4% compared with 2006. This loss was absorbed mainly by Gaz de France, the second main actor on the Belgian market, which registered a market share of 15.2% in 2007. As a result the share of the Suez-GDF Group scarcely changed in 2007: it went from 93.9% in 2006 to 93.4% in 2007. In 2007 the group still had a de facto monopoly in Belgium. The third actor, in order of importance, booked a market share of 6% in 2007.

2.2.1.2. Development of exchanges and hubs

a) Electricity

In 2007, the total volume traded on the Belgian electricity exchange stood at 7.6 TWh, which accounts for nearly 8.5% of the Belgian electricity consumption, estimated at 88.8 TWh in 2007. During the year under review, the total volume purchased on Belpex amounted to 6.8 TWh; the volume sold to 4.9 TWh. This difference between the volume purchased and the volume sold is precisely due to the market coupling and the imports and exports with France and the Netherlands.

The average annual price on the Belpex market in 2007 was €41.8/MWh, while the average monthly price for the first nine months of the year under review fluctuated between €26/MW and €41/MW, prior to the sizeable increase in the last three months of the year (up to €87/MWh in November).

Following the observed price trend and cross-border flows between the Netherlands, Belgium and France, in 2007, the CREG started to examine the functioning of Belpex, when the power exchange had been in operation for about one year.

On the regulatory front, changes were made to the Belpex market regulation aimed in particular at creating a new type of membership to make access to the Belpex DAM more attractive to the smaller actors on the market.

Finally, no sign of any reorientation or shift to less transparent OTC type transactions was identified in 2007, taking into account the growth of volumes traded on the electricity exchange and the number of participants (24 at the end of 2007).

b) Natural gas

As regards the trading of natural gas on the wholesale market in Belgium, trading was carried out chiefly through OTC type of transactions at the Zeebrugge hub. This hub nonetheless co-exists with the Belgian natural gas exchange, APX Gas ZEE, launched in 2005.

- *Zeebrugge Hub*

The liquidity of the Zeebrugge Hub continued to improve in 2007. Membership of the Zeebrugge Hub also increased in 2007: having 70 members at the end of 2007.

The grid operator increased the services offered by introducing the Zee Platform Service on the market in 2007 to enable users of this new service to exchange natural gas without capacity restriction between the four entry points in Zeebrugge. This stage in the development of the Zeebrugge Hub should also promote competition between suppliers on the Belgian market.

This gradual improvement of the liquidity of the Zeebrugge Hub is expected to continue this year, in particular because in February 2008, the grid operator removed the last capacity restraints on the hub.

- *Natural gas exchange*

In the year under review, APX Gas ZEE, the Belgian natural gas exchange launched in 2005, registered a significant increase in the volume traded by comparison with 2006. This improvement in the liquidity of the Belgian natural gas exchange can be explained by the increase of commitments by the members of the exchange, inasmuch as the continental natural gas markets show relatively similar trends, being in a liberalisation process and geared to greater transparency. The volumes traded on the Belgian natural gas exchange nonetheless remain lower than those at the Zeebrugge Hub. Furthermore, the Belgian natural gas exchange had only 13 members, compared to 70 for the Zeebrugge Hub.

2.2.2. The retail market

- *Full liberalisation of the gas and electricity market*

The liberalisation of the energy market in Belgium was carried out in different steps, which varied

depending on the timetable of the regions and the Federal State itself. The year 2007 was nonetheless a turning point, as the entire Belgian gas and electricity market was liberalised as of 1 January (in Flanders, this liberalisation had already been in force since 1 July 2003).

- *Changes of supplier*

In 2007, 5.59% of the end consumers of electricity and 6.9% of the end consumers of gas in Flanders opted to sign a contract with another supplier (based on the number of access points). Switches were carried out essentially during pivotal moments (at the end of old contracts) and were stimulated by the increase in prices and the growing interest paid to this issue (e.g. attention of the media). The change of supplier is free for the end consumer. As soon as the end consumer is sufficiently informed and has found the supplier of his or her choice, the end consumer enters into a supply contract with that supplier.

For the electricity distribution market in Wallonia, the number of customers signing a supply contract continued to increase in 2007, representing in the end one out of two customers. Four out of ten of these active customers opted for a supplier other than the one designated for their area. For the gas distribution market, 52% of the customers had signed a contract by 1 December 2007 (compared with 31% at the beginning of 2007).

The electricity distribution market in Brussels was characterised by a number of salient facts:

- One Brussels resident in ten moved in 2007;
- A very important increase in professional electricity customers (+50%) owing to the more attractive conditions for this type of contract for mixed use (liberal professions, etc.);
- Only 2.3 % of residential electricity customers changed supplier; this is due to the type of contract and the scarcity of suppliers present on the market;
- Only 2.4 % of professional electricity customers changed supplier;
- Only 2.5 % of residential gas customers changed supplier; this is due to the type of contract and the scarcity of suppliers present on the market.

2.2.3. Infrastructure

2.2.3.1. Tariff developments

a) Electricity

- *Transmission and distribution tariff developments*

In comparison with 2006, the transmission tariffs (exclusive of surcharges and VAT) resulted in a further substantial fall in the costs for grid users. This fall varies between 9.53% and 12.15%, depending on the voltage level. This decrease in costs has continued since 2002, oscillating between 52.77% and 54.35%.

For distribution, the tariffs applied in 2007 appeared on average to be 2.31% higher for household customers (3,500 kWh), compared with 2006. On the other hand, industrial customers are benefiting from a slight fall in the tariffs, of about 0.5% for consumption of 1,250 MWh per year and 1.8% for consumption of 30 MWh per year. Furthermore, the average distribution tariffs remain considerably lower than in 2003, the year in which the CREG was given the authority to approve such tariffs, and where applicable reject cost resulting in a decrease of distribution tariffs to the benefit of consumers.

- *Introduction of multi-annual annual tariff setting for transmission*

As regards the electricity transmission tariffs, the year 2007 was characterised by the adoption of the Royal Decree of 8 June 2007¹², at the proposal of the CREG¹³, which introduced a new, multi-annual tariff setting method.

The new system guarantees the transmission system operator, for a regulatory period of four years, a total income that is sufficient to carry out the tasks required by law and obtain a fair profit margin in return for the capital invested in its grid. This income for each year of the regulatory period is divided into “controllable” costs, i.e. costs over which the system operator exercises a direct control, and “non-controllable” costs, which are listed in the aforementioned Royal Decree of 8 June 2007.

The most striking feature of this new multi-annual tariff setting system is that, contrary to the previous ‘cost-plus’ system, the transmission system operator is offered an incentive to boost profits via the balance from the controllable costs: every year, the difference between the actual controllable costs and the budgeted costs is granted to the transmission system operator. The cost reduction achieved by the transmission system

¹² Royal Decree of 8 June 2007 on the rules for fixing and controlling the total income and the fair profit margin, the balance between costs and revenues and the basic principles and procedures for the proposal and approval of tariffs, the ratio and control by the national electricity transmission grid operator, *Moniteur belge* [Belgian Official Gazette], 29 June 2007.

¹³ Proposal (C)061005-CDC-190/28.

operator must ultimately lead to lower tariffs for grid users. It is important to point out that an incentive to increase investment is also incorporated: when tangible fixed assets are taken out of service, as of 1 January 2008, the surplus value, resulting from the relevant assets from the initial regulated asset is charged against the total income to be covered by the tariffs, provided the corresponding amount of this capital gain is booked as an investment reserve and therefore remains within the company, available to be used as a source of self-financing.

This tariff setting system entered into force in January 2008 and shall apply until 2011. The transmission tariffs for 2007 will thus have been the last to be fixed on a “cost-plus” basis for a period of one year. The introduction of the new multi-annual tariffs should provide greater stability and thus facilitate access to the grid.

- *Change of the method used to establish the bonus/malus for distribution tariffs*

An important change for distribution tariffs in 2007 lies in the calculation of the bonus/malus for reassessing the tariffs for electricity distribution during the previous year. In several judgements of 27 February 2007, the Court of Appeal in Brussels criticised the previous method used by the CREG, which had to comply with these judgements. From now on, the operating result may no longer be distinguished from the bonus/malus. Furthermore, half of this bonus/malus, which must be established between the result arising from the application of the tariffs approved by the CREG and the budgeted result (fair profit margin), must be charged to the distribution grid and half to the end user. The CREG has complied with these judgements of the Court of Appeal and consequently applied these principles in establishing the bonus/malus resulting from the application of the tariffs in 2006. These judgements also had an impact on the way in which the 2008 tariffs were established at the end of 2007. For different reasons¹⁴, the CREG has nonetheless regretted this jurisprudential development that will necessarily lead to tariff increases to the detriment of consumers.

- *Judgements concerning the distribution tariffs*

Beyond the aforementioned judgements of the Court of Appeal in Brussels, 2007 was marked by the – at times fundamental – challenge of the regulation on the distribution tariffs by the same court. The Court has actually rendered several judgements in proceedings introduced by the distribution system operators against tariff decisions of the CREG. The Court has in particular proved very severe in respect of certain discretionary powers of the CREG, which gives rise to the fear that it will no longer be able to fulfil its legal tasks properly. According to the Court, the CREG

¹⁴ Cf. Annual Report 2007, n°2.8.1.

does not have any regulatory competence as regards determining depreciation rules; its authority to determine the profit margin is limited; it has accepted bookkeeping as the cornerstone of tariff setting; it has only limited powers to assess the reasonable nature of costs; and as regards the distribution of gas, it is no longer allowed to assess the reasonable nature of costs imposed by another competent authority.

These judgements have inevitably led to tariff increases which have been felt as of 2008.

b) Natural gas

- *Transmission, storage and distribution tariff developments*

After having fallen constantly for five years, the transmission tariffs for natural gas stabilized in 2007 and increased with 2% compared with 2006. This increase remains modest in the light of the major investments that have been made to improve prevention and security on the grid, cover the increasing demand for natural gas and offer users new services. This low cost has moreover been confirmed by an external study¹⁵ according to which Fluxys is below the European average for transmission costs. However, according to another study conducted by ERGEG¹⁶, these results should nevertheless be qualified .

As far as the tariffs for storage in liquid form are concerned, these continue to fall since five years and fell by a further 9% between 2006 and 2007. However, the tariff for aquifer storage rose by 11% as a result of investments in the expansion of the Loenhout storage facility with a view to increasing the volume stored (+17%) and the emission capacity (+ 25%) and because of the operating costs of the Poederlee storage project.

In comparison with 2006, the distribution tariffs applied in 2007 seem on average to be 3% lower for household customers (22 MWh/year) and 9% lower for industrial customers (36,000 MWh and 12 MW peak). For business customers (2.300 MWh/year), on the other hand, an average rise of 3% was observed. As regards household customers in particular, the distribution grid tariffs remain even, on average, considerably lower than their level in 2004, the year in which the CREG was given authority to approve those tariffs. Since 2004, the CREG has rejected significant amounts in costs, resulting year by year in a drop in the distribution grid tariffs to the benefit of consumers.

- *Introduction of a new multi-annual tariff setting for the transmission and a new method for establishing the bonus/malus for the natural gas distribution tariffs*

¹⁵ Cf. Table 17.

¹⁶ 'Gas Transmission Tariffs. An ERGEG benchmarking report', 18 July 2007.

As access to the gas transmission grids is regulated in accordance with the same general tariff principles as those applicable to electricity, except for certain reservations, regulatory changes that introduce a new, multi-annual tariff setting for 4 years as of 1 January 2008, also occurred in 2007 for the transmission of natural gas.¹⁷

Similarly, as regards the distribution tariffs, the method used to establish the bonus/malus underwent a major change after the judgements of the Court of Appeal in Brussels of 27 February 2007. (Cf. the developments on this matter discussed under the point on electricity).

2.2.3.2. Investments in the transmission grid

a) Electricity

Several decisions geared to strengthening the electricity transmission grid were taken in 2007. In January 2007, for instance, it was decided to strengthen the Belgian-French interconnection by converting the Chooz (F) Monceau line to 220 kV across its entire length and the installation of a phase-shift transformer at the Monceau substation. Elia also brought two 150 kV connections on line (21 km between Monceau and Thy-le-Château, and 0.5 km between Keerken-Lokeren Vijgenstraat) and strengthened a 150 kV connection (5 km between Trivière and Ville-sur- Haine).

Furthermore, in February 2007, the five regulators of the Central-West European region published their action plan for the 2007-2009 period with the aim of accelerating the regional integration of the electricity markets. This plan includes the elaboration of a regional investment plan for the transmission grid.

b) Natural gas

- *The second rTr project*

As regards natural gas, the construction of the compression station in Zelzate at the

¹⁷ Royal Decree of 8 June 2007 on the methodology for establishing the total income comprising a fair margin, regarding the general tariff structure, the basic principles and procedures on tariffs, the procedures, the announcements of tariffs, the annual reports, the bookkeeping, the cost control, the differences in income between operators and the objective indexation formula referred to in the Law of 12 April 1965 on the transmission of gaseous and other substances by pipeline, *M.B.* [Belgian Official Gazette], 19 June 2007.

interconnection between Belgium and Germany was in its final stage at the end of 2007. However the transmission grid operator, Fluxys, has fallen seriously behind schedule in the laying of an additional pipeline from Eynatten. This strengthening is not only important for Belgian transit activities, but is also necessary to be able to safeguard national gas supply in the future.

- *The Blaregnies/Taisnières interconnection*

In March 2007, the CREG decided, together with the French regulator (CRE), to set up a joint working group, in conjunction with the Belgian (FLUXYS) and French (GRTgaz) transmission gas operators. This working group aims to improve access to France via Belgium. These prospects for additional transmission capacity and services offered by FLUXYS to stimulate the use of the transmission grid, helped to double the number of shippers who have subscribed to access capacity in Taisnières, increasing from 6 to 12 as at 1 December 2007.

- *Expansion of storage capacity*

The construction of a fourth LNG storage tank and additional regasification facilities at the LNG terminal in Zeebrugge entered its final phase in 2007. However, this new capacity has already been fully subscribed to, so that in December 2007, FLUXYS LNG launched a new open season for additional LNG terminalling capacity. Depending on the result of this open season, additional capacity may be made available from 2015-2016 onwards.

As regards the expansion of storage capacity in Loenhout, investments started in order to increase this capacity by 15% to a useful volume of 700 million m³ and extend the injection and emission capacity. This additional capacity is scheduled to come into operation towards the spring of 2010.

- *Study on the halt to investments in the L-gas market and the switch to H-gas*

As for investments in natural gas, it is to be noted that in September 2007, the CREG made, in conjunction with FLUXYS, a study on the halt to investments in the L-gas market and the switch to H-gas.¹⁸ This study developed, on a technical level, the recommendations already made by CREG in the proposal of indicative plan for natural gas supply for the 2004-2014 period.¹⁹ In essence this proposal recommended a switch of end customers from L-gas to H-gas to obtain additional capacity and thus remedy the foreseen increasing shortage of peak capacity in the L-gas transmission grid as from the winter of 2008-2009. The study of September 2007 examined the

¹⁸ Study (F)070913-CREG-691 (available at www.creg.be)

¹⁹ Proposal (F)040923-CREG-369 (available at www.creg.be).

potential, procedures and cost of such a switch, while announcing other steps under a more general study of this problem. This step-by-step plan aims in particular to inform the market players about zones which, in the view of the transmission system operator, could be the first to come into consideration for a switch to H-gas.

- *Exemptions of Article 22 of the Gas Directive – Poederlee Gas Storage*

It is to be noted that the exemptions of Article 22 of Directive 2003/55/EC are not applied in Belgium. The only case to be indicated is an application from POEDERLEE GAS STORAGE (PGS) for an exemption provided under Article 22 as regards the tariff methodology and the right of access for an underground storage site in aquifer in Poederlee. The application submitted by PGS, 25% of which is owned by FLUXYS and 75% by GAZPROM, related to the allocation of the total storage capacity to GAZPROM for a 25-year period. The CREG issued a negative opinion based on the persistent uncertainty as to whether or not PGS met the criteria that by law have to be fulfilled to be able to benefit from an exemption under Article 22. The CREG also felt that FLUXYS had not used all available means to enable the development of the storage facility without having to call upon the exemption requested. In the meantime, the project was interrupted because, according to FLUXYS, it did not meet the envisaged economic criteria.

2.2.3.3. Allocation of capacity

a) Electricity

- *Reorganisation of the capacity allocated on the Belgian-French interconnection*

In 2007, the Management Board of the CREG authorised the reorganisation of the capacity allocated over the various periods in time in favour of daily capacity for the Belgian-French interconnection.²⁰ In April 2007, the Management Board took a decision authorising the introduction of a mechanism for the allocation of intraday capacity at the Belgian-French interconnection.²¹

- *Refusal to modify the rules governing the monthly and annual auctions*

In December 2007, the CREG took a decision to reject the proposal put forward by the transmission grid operator ELIA to alter the rules governing the monthly and annual auctions of

²⁰ Decisions (B)070412-CDC-677 and (B)071122-CDC-729 (available at www.creg.be).

²¹ Decision (B)070412-CDC-678 (available at www.creg.be).

available capacity, because this did not improve upon the previous version of the auction rules.²² The conditions of suspension and the limitation of the operator's liability in particular were deemed unacceptable.

- *Announcement by ELIA of a reduction of the minimum capacity guaranteed by the TSO on the interconnection with France*

Finally, in December 2007, ELIA announced the guaranteed minimum capacity which the system operators undertook to allocate throughout 2008 at the interconnection with France, i.e. 1600 MW from France to Belgium, corresponding to a reduction of 100 MW compared to the minimum value for 2007, and 600 MW from Belgium to France.

The CREG issued a press release denouncing this reduction of the minimum capacity which the system operators undertook to allocate throughout 2008, although the interconnection had been strengthened in 2007, and further strengthening was in progress. The guaranteed capacity from Belgium to France is only 600 MW, whereas the physical capacity of the interconnection is about 5000 MW. The CREG considered that the method for determining the capacity used is not very transparent, and feared that it may be discriminatory and in violation of European Regulation 1228/2003 and its annex, in particular by transferring internal congestions to the borders.

Consequently, the CREG asked the grid operator to submit, by 1 March at the latest, the method of calculation and all the elements used to establish the values of 1600 MW and 600 MW. The CREG also asked ELIA to make every effort to respect the previous value of 1700 MW, in particular during the summer of 2008, and to study, by 1 March 2008, the procedures for implementing, exceptionally, a preventive re-dispatching.

b) Natural gas

In spite of the positive results of the open seasons and the fact that a number of investment initiatives are on the point of implementation, the transmission grid operator, FLUXYS, did not manage to make up for its delay in proposing new transmission capacity in time. The delays and reviews of major investment projects mean that the shippers are not always able to subscribe for additional entry capacity, so that a situation of contractual congestion has emerged on the natural gas market in Belgium. This situation of contractual congestion applies for both the national market and transit activities. For instance, as long as the vTn 2 project has not been put in place, additional natural gas supply from Germany via Eynatten and Zelzate to the Belgian natural gas

²² Decision (B)071211-CDC-733 (available at www.creg.be).

market is impeded. This situation reveals the limits of the “*First Come First Committed*” (FCFC) allocation system currently in use in Belgium and bears witness to the need for an alternative system leading to a better balance between the long- and short-term allocations corresponding to the needs of the grid users.

On the basis of the current developments, adequate capacity should again be available in 2012, even if uncertainties persist after this date. Until then, a suitable congestion policy must be implemented. The CREG has complained repeatedly to FLUXYS about the lack of both investments and a suitable congestion policy. However, the incentives provided have not yielded the hoped-for results, at least not in the short term.

2.2.4. Regulation / unbundling

- *Role of the CREG*

Two changes occurred in the powers of the CREG in 2007:

- In exceptional circumstances, it may now decide straightaway to review the rules on the total income required to fulfil the legal and regulatory obligations incumbent upon the natural gas transmission system operator, the storage installation operator and the LNG installation operator (Law of 21 December 2007, ‘Moniteur belge’ [Belgian Official Gazette] of 31 December 2007).
- The CREG must henceforth submit a reasoned report every year to the Minister for Energy and the transmission system operator, indicating whether the prices offered to the transmission system operator for the provision of auxiliary services are evidently unfair or not (Law of 16 March 2007, ‘Moniteur belge’ [Belgian Official Gazette] of 26 March 2007). Previously, if it noted that the prices offered to the electricity transmission system operator for the provision of auxiliary services were not compliant with the European practices, it had to refer the matter to the Competition Council.

- *Penalties imposed by the CREG*

In 2007, the CREG initiated, on several occasions, the administrative fine proceedings provided under Article 31 of the Electricity Law and Article 20/2 of the Gas Act, in particular under the tariff obligations imposed on gas and electricity distributors system operators. These dossiers have not led to the imposition of a fine, however.

- *Role of the CREG in the appointment of the transmission system operator*

Article 15/14, §2, of the Gas Law entrusts the CREG in particular with the task of supervising and monitoring the laws and regulations relating to the natural gas market. This task requires the CREG in particular to examine the extent to which the grid operators fulfil, in practice, the obligations stipulated in the Gas Act, including the unbundling conditions.

No permanent grid operator had yet been appointed in 2007, but FLUXYS was the provisional grid operator appointed as of right. This status implies in particular that only a limited number of unbundling conditions need be met by comparison with the grid operator appointed in a permanent capacity.

On the appointment of the permanent grid operator, Article 8 of the Gas Law stipulates that the CREG must first issue an opinion to the Minister on the matter. In June 2007, the CREG did issue such an opinion once Fluxys had applied for the position of the natural gas transmission system operator, the storage installation operator or the LNG installation operator.²³ The CREG examined the application and issued a negative opinion on the appointment of FLUXYS as operator of the LNG terminal. On the other hand, it issued a positive opinion, subject to certain conditions, on the appointment of FLUXYS as the operator of the natural gas storage facility and as the operator of the natural gas transmission grid. The Minister has not appointed a permanent grid operator to this day. It is true that the Gas Law does not stipulate any specific limit in time for the appointment of a permanent grid operator.

- *Unbundling*

Gas transmission:

Fluxys, as the provisional operator of the natural gas transmission grid, has been legally separated from DISTRIGAZ since 2001; the two have an identical shareholding structure (Suez/Tractebel 57.25%, Publigaz 31.25%; the rest quoted on the stock exchange). Due to the merger and the commitments which were accepted in the European decision, the shareholding structure will undergo fundamental changes in both undertakings. Pursuant to paragraph 53 of these commitments, Suez-Gaz de France and Publigaz “shall each hold an identical stake in Fluxys, corresponding to a maximum of 45% of the capital of this company; the rest, apart from the golden share, being quoted on the stock exchange.” In 2007, the merger had not yet been carried out,

²³ Opinion (A)070628-CDC-697.

however, and the change in the shareholding structure of FLUXYS has not taken place to date.

Gas and electricity distribution:

There were no major changes with regard to unbundling at distribution level in 2007. The most important changes on this front took place in 2006.

However, given the trend among distribution system operators to create “societies d’exploitation” (“operating companies),” the Flemish Government imposed in July 2007 legal conditions applicable to distribution system operators resorting to this type of companies. These are based on the principle that such “operating companies” must meet the same independence requirements as the system operators themselves.

2.2.5. Security of supply

2.2.5.1. Investment developments

- *Electric power generation*

The total installed generation capacity amounted to 16,363 MW in 2007, compared with 16,150 MW in 2006.²⁴

As to investment perspectives in generation units for the 2008-2012 period, 990 MW are under construction, 2,509 are authorised²⁵ and 1,821 MW are planned.²⁶

In September 2007, the CREG took the initiative to make a study on the insufficient electricity generating capacity of Belgium.²⁷ The study drew attention to the increasing risk that it will no longer be possible to permanently cover the demand for electricity in Belgium over the years ahead, which Belgium is likely to face. For example, in the main scenario, the study forecasts that by 2012 there will be a need for additional generating capacity of 2,000 MW base units. The study lists the possible ramifications of the shortfall in generating capacity and recommends various measures in the short and medium term.

²⁴ Federal Public Service Economy, SMEs, Self-Employed and Energy. Provisional data.

²⁵ These 2509 MW have been authorised, but construction has not started yet. These are projects for which a domain concession (off-shore wind farm) or a generation permit (other power stations of more than 25 MW) have been granted.

²⁶ For which an application for a permit or domain concession is still being examined.

²⁷ CREG, Study (F) 070927-CDC-715.

Finally the first study on the outlook for electricity supply for the 2008-2017 period (the so called “prospective study”),²⁸ drawn up by the Directorate General for Energy of the Federal Public Service Economy, had not yet been published at the time that this annual report was being drawn up. The same applies to the study on the outlook for gas supply.

- *Storage capacity*

In 2007, the CREG reiterated the considerable shortage in storage capacity on the Belgian market, in particular in its opinion²⁹ on the application by Poederlee Gas Storage for an exemption as regards the tariff methodology and the right of access to an underground storage site in aquifer situated in Poederlee.

Only the expansion of the capacity of the underground storage in Loenhout started in 2007. The aim of the new investments is to increase storage capacity by 15%, over the 2008-2011 period, to a useful volume of 700 million m³ and extend the injection and emission capacity. This additional capacity is scheduled to come into operation towards the spring of 2010.

In addition, the seismic research carried out in May 2007 to assess the possibility of another underground storage facility in Poederlee did not lead to any decision to start construction of a second underground storage facility. This investment project actually did not meet the economic criteria fixed by the system operator, which induced the latter to put an end to this investment project.

- *LNG*

The construction of a fourth LNG storage tank and additional regasification facilities at the LNG terminal in Zeebrugge entered its final phase in 2007. As a result, the emission capacity will be doubled in 2008 from 4.5 to 9 billion m³ (n)/year. This expansion is the result of an open season in 2003-2004.

The total capacity of the LNG storage terminal (slots, storage, emission) has already been subscribed to for several years by three shippers. The new capacity is scheduled to come into operation in the course of this year.

In 2007, Fluxys LNG also launched a new open season for additional LNG terminalling capacity. Depending on the results of this open season, additional capacity can be made available from

²⁸ The Law of 1 June 2005 replaces, in the Electricity Law, the indicative programme for power generation, the elaboration of which had been entrusted to the CREG, by a study on the outlook for electricity supply, known as a prospective study, to be conducted by the Directorate General for Energy.

²⁹ CREG, Opinion (A)0704419-CDC-683

2015-2016 onwards.

- *Investments in the natural gas transmission grid*

Although the open seasons produced positive results and a number of investment initiatives are on the point of implementation, the transmission system operator had difficulties to provide new transmission capacity in time.

As a result of the delays and reviews of major investment projects the shippers were not always able (and continue to be unable) to subscribe for additional entry capacity.

Contractual congestion situations have thus been observed for both the national market and transit activities.

The CREG has repeatedly emphasised the delay in the realisation of the investments in the transmission grid and the need to implement a suitable congestion policy. However, the incentives provided have not yielded the hoped-for results.

For instance, as long as the vTn 2 project has not been carried out in its entirety, the absence of the possibility of additional natural gas supply at Eynatten, from Germany, constitutes a barrier to entry to the Belgian natural gas market. This reinforcement is important for the Belgian transit activities, but also necessary to guarantee the national supply of natural gas in the future.

- *Investments in the electricity transmission grid*

As regards the main expansions of the transmission grid in 2007, the strengthening of the 220 kV line between Monceau (B) and Chooz (F) – was completed with the being operational of a phase-shift transformer at the Monceau substation.

Depending on the solution to technical problems which occurred unexpectedly, the the three phase-shift transformers on the Belgian 380 kV grid at the border with the Netherlands are expected to be operational by the end of 2008. These transformers will make it possible to control better the flows in Belgium (North – South and South – North) so as to improve security of the grid and release more interconnection capacity.

Depending on the level of imports, a certain number of capacitor banks and of 380/150 kV transformers will also be added in order to make Belgium more independent from the domestic generating facilities. Finally, the long-term strengthening of a 380 kV internal line between Gramme and Massenhoven, as well as the reinforcement of the interconnection between the Ardennes (B)

and Lorraine (F) are also being examined with a view to increase the potential for transactions between France and Belgium.

2.2.5.2. Diversification of sources and routes

- *Electricity*

In 2007, the electric power generated in nuclear facilities represented a little more than 55% of all the electric power generated by the generation units connected to the ELIA grid. The corresponding part for natural gas amounted to nearly 31%.

In terms of capacity, in 2007 nuclear power generation on the one hand and the CCGTs and gas turbines on the other hand represented nearly 37% resp. 26% of the total installed capacity of power stations connected to the Elia grid.

Finally, as regards incentives to boost electric power generation, Article 7 of the Electricity Law provides for several support measures to promote renewable sources of energy. To this end, it is worth mentioning in particular a system of green certificates for green energy generated by the offshore wind farms on the North Sea, the partial financing by Elia of the cost of the underground cable intended for the offshore wind farms on the North Sea, the support mechanisms for the benefit of holders of domain concessions, where deviations from generation schedules are larger because of the uncertainties linked with wind farms and the support measures in the event of withdrawal of domain concessions for reasons other than a form of negligence on the part of the concession holders.

There are also different support measures at regional level, in particular green certificate systems.

- *Natural gas*

Belgium remains totally dependent on imports of natural gas.

Natural gas suppliers can choose from among a series of entry points to supply their customers with H gas. Gas customers who use L gas are supplied directly from the Netherlands or indirectly via the Blaregnies interconnection point with France.³⁰

Natural gas is imported mainly via the Zeebrugge entry zone, where the gas hub is also located for short-term gas trading. Taking into account imports of LNG, 47,2% of Belgian natural gas demand

³⁰ It is worth pointing out that, as regards the L gas market, there is an investment stop until further order.

is met via Zeebrugge.

The relative importance of LNG in the Belgian supply nonetheless diminished considerably in 2007, owing in particular to the end of the historical supply contract with Algeria and the new supply contract with Qatar, which is relatively less sizeable.

Supplies via the east entry zones increased in 2007 (to 16.6%, against 13.3% in 2006) and the market signs indicate that this trend is set to continue.

Finally, natural gas suppliers active on the Belgian market have a differentiated supply portfolio in which long-term contracts concluded directly with natural gas producers make up by far the largest component.

2.2.6. General conclusions relating to the legal framework

In 2007, the CREG took a series of initiatives to improve the current legislation, relating in particular to the promotion of competition on the markets, the opening of access to the grids, and the strengthening security of supply.

The CREG has moreover repeatedly underscored the need to be vested with the powers and means necessary for the full implementation of European directives, and in particular the task conferred on the regulators to ensure effective competition and an efficient functioning of the natural gas and electricity markets, in particular through continuous monitoring of the activities subject to competition, both as regards pricing and the practices and behaviour encountered in the field. The adoption of the Law of 8 June 2008 comprising various provisions is a positive sign in this sense, as it provides for the strengthening of the powers and rights of the regulator, charging it with the supervision of transparency and competition on the natural gas and electricity market, the monitoring of prices on these markets, the essential interests of consumers as well as the proper fulfilment of the public service obligations by the companies concerned. These regulatory advancements are fully in line with the proposals contained in the third European legislative package under review.

2.3. Main issues dealt with by the regulators

2.3.1. The CREG

As it is not possible to separate from point 2.2., the specific role of the CREG that is broached by the questions of point 2.3, the reader is requested to refer to the answers in point 2.2.

As regards the retail market and consumer protection, the powers of the CREG are relatively limited since the supervision of this market in particular falls under the purview of the regions. Furthermore, as to the evolution of prices on the retail market, no breakdown of the average gas and electricity prices could be established for Belgium in 2007, as the Eurostat data were not yet available for that year.

However, the supervision of costs of transmission and distribution system operators and the approval of their tariffs undoubtedly confer on the CREG an essential role in the protection of consumers . In the course of 2007, no fewer than 51 decisions were taken by the CREG to exercise this power.³¹

As regards gas and electricity prices, the CREG also assumes the task of collecting the federal contribution and sees to the proper application of specific tariffs for protected customers. In the course of 2007, the CREG continued to perform these tasks.

It is also worth noting the study carried out by the CREG³², at the request of the Minister for Energy, on the causes and ramifications of the gas and electricity price increases that had been announced by ELECTRABEL CUSTOMER SOLUTIONS S.A. on 15 June 2007, and on the measures to remedy these increases. The CREG study of 27 July 2007 concluded that the reasons invoked by Electrabel for the increase of the price of natural gas (+17%) were often, but not always, pertinent. Furthermore, this study underscored that, upon the full liberalisation of the market in Brussels and in Wallonia on 1 January 2007, elements indicated that Electrabel Customer Solutions had fixed the prices of natural gas at a very low level, possibly with a view to eliminating competitors from the market or of creating an entry barrier (*predatory tariff setting*). Owing to lack of competence to supervise and intervene on the one hand, and lack of cooperation of Distrigas on the other, the CREG was not able to prove possible abuses of dominant position. Nevertheless, the aim of the CREG study of 27 July 2007 was to enable other authorities that are

³¹ Annual Report 2007, Annex, pp. 61ff.

³² Study (F)070727-CDC-704 (available at www.creg.be). A press release (n°56) summarising the study is also available at <http://www.creg.be/pdf/Presse/2007/compress01082007fr.pdf>.

also in charge of this matter, such as the competition authority, to draw inspiration from the observations and conclusions of this study, so as to see their own investigations through. Furthermore, this case has enabled the CREG to insist even more on the need to be entrusted with the task of establishing a permanent monitoring of the gas and electricity markets. An important step will be made in this direction with the Law of 8 June 2008 comprising various provisions.

Finally, it is worth noting the daily intervention of the CREG to deal, on a voluntary basis, with questions raised by the consumers, on the difficulties that arise from the liberalisation of the gas and electricity market. In the absence of an ombudsman service, though created by the Law of 16 March 2007, in most cases, the CREG has to advise consumers to address their questions to the Information Department of the Federal Public Service Economy.

2.3.2. VREG

2.3.2.1. Tasks of the VREG relating to the liberalisation of the energy market

The energy market in Flanders has been fully liberalised since 1 July 2003.

As the supervisory authority, the VREG is intent on facilitating the establishment and implementation of processes for the proper and efficient functioning of the market, for strengthening competition and playing a leading role by assessing the working of the market and correcting it as and when required. Discussions with system operators and suppliers have revealed a need for a macro-economic analysis of the energy market as well as a need to analyse certain obstacles that stand in the way of its working efficiently.

These needs have prodded the launch of a market model study, the first result of which was an advisory document published by the VREG in the beginning of 2006 entitled "Towards a market model for the Flemish energy market." This study, which was carried out in cooperation with an important academic and theoretical partner, provides an initially overall view of the organisation of the Flemish energy market and includes a description of the difficulties that suppliers and grid operators have to face at present.³³

Moreover, the VREG issues green electricity and co-generation certificates to facilities based on renewable energy and co-generation (quality co-generation put in operation after 1 January 2002).

³³ On the subsequent use of this study, cf. b, *infra*).

Flanders has 100 such facilities using co-generation at present.

The VREG thus implements a policy of green and co-generation certificates and processes individual requests, facilitates the market of certificates thanks to the dissemination of information (statistics on its website), participates in consultation platforms to promote renewable sources of energy and co-generation (for example, co-generation and organic co-generation platforms), and receives visitors with specific questions for complex matters. The VREG also intervenes to settle disputes relating to connection problems, with a view to prepare the grids for a more decentralised generation, e.g. for new regulations on connection: the system operators are asking that some attention be paid to the technical characteristics of decentralised generation, so that it can constitute a support for the grid.

To prepare the arrival of many small generators, the VREG also disseminates information on its website, publishes certificate application forms adapted to small-sized facilities (e.g. photovoltaic installations and, in future, micro co-generation as well), participates in seminars intended for installers, in particular to provide practical tips on the administrative steps in order to be able to benefit from an installation.

At the international level (Association of Issuing Bodies), the VREG takes part in consultations for an efficient implementation of, in particular, “GO for heat” or for the international trade of these GOs.

2.3.2.2. Progress of the “market model for the Flemish energy market” project

After the first phase of the market model had been implemented by the VREG in cooperation with an external consultant, a consultation phase was launched. Companies in the energy sector reacted to the observations of the first phase.³⁴

On the basis of these reactions, on 21 November 2006, the VREG sent an opinion to the then Flemish Minister for Energy, Mr Kris Peeters.³⁵ The latter entrusted the VREG with the task of continuing the study in cooperation with the energy sector, which had to commit itself thereto. The clarification of agreements on the approach and financing of the study and the selection of a consultant assigned to supervise the study extended over a large part of 2007.

³⁴ It is still possible to consult these texts (in Dutch) at http://www.vreg.be/nl/03_algemeen/06_consultatie/02_afgesloten/01_marktmodel.asp.

³⁵ Opinion of 21 November 2006 relating to the continuation of the study “Towards a market model for the Flemish energy market” and reactions from the consultation round on the first phase of this study. This opinion, in Dutch, can be consulted at <http://www.vreg.be/vreg/documenten/adviezen/ADV-2006-4.pdf>.

The second phase started in October 2007, under the aegis of a project committee and was subdivided, in practice, into four work paths:

- The first path, entitled “Description of the current market model,” had to establish a common defined image of the current market organisation. The term “market organisation” or “market model” refers to the “entire regulatory framework (at European, federal and regional level), the agreements concluded in the sector (formally, in the UMIX body, but also more informally) and the contractual and financial currents that determine how the market functions alongside the physical and information flows.” Owing to the rather organic nature of the current market model, each company operating on this market naturally has its own view on how the market functions, but an overall view defined in common is lacking. Finally, the first path had to draw up a list of the problems affecting the current market model.
- Then, a second path, entitled “Market roles” had to be initiated to find a solution to the main problems identified. This path is geared to eliminating, where appropriate, vague or ambiguous elements in the current model (for instance, when the market roles are not yet defined with sufficient clarity or when several possibilities are still proposed for the same action/same role) by opting for an efficacious solution at market level. Here, the current market model can be simplified and made more efficacious from the macro-economic point of view in cooperation with the market actors. The aim is to reduce costs that should ultimately lead to a reduction in the price charged to the end user. In fact, the consultation after the first phase showed that there was more substantial support to improve the current market model than to develop a new one.
- Paths 3 (concerning the data quality) and 4 (concerning “smart meters”) were also launched at the outset of this phase. Path 3 “Data cleansing” aims to find a solution so as to solve and avoid data file pollution. Furthermore, it is necessary to move rapidly by introducing the necessary control processes.
- Path 4 entitled “Metering infrastructure” is a study process geared to contributing to an assessment of whether the implementation of “smart computers” is desirable and feasible. In concrete terms, such feasibility must be justified from a technical and economic point of view.

In parallel to this study, conducted by the VREG and companies operating in the energy sector, the VREG also defined a path for the market actors, to inform the representatives of customers and to involve them in the study. Owing to the technical and detailed nature of the discussions conducted in these paths, these representatives could not really take part therein.

What is the current situation of the study?

Attaining the objective of path 1 proved far more difficult than initially thought and expected. It was virtually impossible to rely on current documentation, and the “confusion of language” when defining a common vision of the market model proved more serious than expected. The number of sessions planned was widely exceeded and the objective has so far been reached only for the processes deemed the most problematic.

Path 3 also unfolded otherwise than planned. The quality of the data is closely dependent on the company processes and databases and on market processes. The company systems could not, however, be analysed under this study and attention was consequently focused on the data processes as a source of data problems. This situation led to another list of problems in addition to that drawn up in path 1.

Path 4 was the clearest and most independent process. A common view was developed as to the options that could be featured in the next generation of natural gas and electricity meters, likewise qualified as “smart meters.” This term was attributed to them because these meters will have more functions than the current ones and will be readable from a distance. An independent costs/benefits study financed by the VREG is currently under way, based on the works of path 4, so its results will be re-examined in connection with path 4.

Path 2 must still get under way, with input from paths 1 and 3.

As to the future, continuing the study – and in particular paths 1 and 2 – as initially defined would not lead to the desired results in due course. Furthermore, the works carried out in path 1 and 3 have also made it possible to develop points of view and certain ideas. It was consequently decided to entrust the conduct of the study to a new project committee composed of CEOs, the decision-makers of the different companies concerned. This committee met formally for the first time at the end of April 2008. Proposals were broached to continue the works of path 1 according to an adjusted methodology, to divide the future path 2 into a long-term strategic project geared to a common view of a future market model, and an operational project in the shorter term so as to be able to correct certain problems in the current market model. The decision on these proposals will be taken in the beginning of June 2008; the study could then continue on new bases. Consequently, the results of this phase will probably not be available before the end of 2008.

On 4 April 2007, the Flemish minister responsible for energy approved the Technical Regulations for gas and electricity distribution. These are updates of the current technical regulations. Attention was focused chiefly on the harmonisation with the other regions and with current agreements

relating to message traffic and access regulation. The VREG has also worked on improving the allocation process in consultation with the system operators, Elia and Fluxys.

All the grid operators in the Flemish Region approved the uniform access regulation, which thus entered into force at all levels in the beginning of 2007. An initial assessment of whether this new access regulation is applied correctly, and more specifically whether the fixed system of responsibilities functions properly, will be carried out in the course of 2008. An analogous uniform access regulation will be established in future for the natural gas distribution grid too.

2.3.3. CWaPE

2.3.3.1. Liberalisation of the energy market

The energy market in the Walloon Region was fully liberalised in 2007, without any major incident on the whole, thanks to the meticulous preparation and anticipation of delicate situations by most of the parties concerned who, under the aegis of the CWaPE, deliberated constructively on the problems pending during meetings christened “Monitoring committee of the total opening of the markets.”

Noting that the main frustration with liberalisation stemmed from the “quality of customer service” of the suppliers, at the end of 2007 the CWaPE initiated systematic inspections among the market actors to verify the procedures and means deployed to meet their legal obligations.

Although they did not always fall under the purview of the CWaPE, the many complaints lodged by private individuals with the regulator were processed, in cooperation with the federal consumer protection department (Directorate General Control and Mediation of the FPS Economy).

The liberalisation of the gas and electricity markets was accompanied by new public service obligations. In 2007, the CWaPE issued opinions and proposals concerning public service obligations of a social nature. It has moreover followed closely the “multi-vendor” IT system development project as regards budget meters (meters with a pre-payment function). The year 2007 was also marked by the success of the negotiations, followed by the CWaPE, initiated by the grid operators for the introduction of budget “gas” meters on the market.

2.3.3.2. Grid activity developments

In 2007, the CWaPE intervened also in grid activity developments. During the initial appointment of

grid operators in January 2003 (electricity) and in October 2004 (gas), the Walloon government had opted for a limited appointment in time in the different municipalities, owing essentially to problems with the right of use or of ownership of their grid. These appointments, limited to 1 January 2006 for 33 municipalities for electricity, were extended until 30 June 2007, in order to concur with the same expiry date specified for 5 municipalities for gas. The Walloon government consequently re-launched an appointment procedure for all these municipalities in the beginning of 2007. The CWaPE analysed the various applications in detail and, depending on the case, made proposals for appointment again limited in time (31 December 2010) or concurring with the 20-year term granted in 2003, i.e. 26 February 2023.

Nevertheless, an initial major revision of the 3 Technical Regulations for the electricity (local transmission and distribution) and gas (distribution) grids and access thereto was carried out after the required consultations with the grid operators and other actors. These updated regulations were adopted by the Walloon Government on 24 May (electricity distribution and local transmission) and 12 July 2007 (gas distribution).

Finally, the CWaPE conducted a(n) (unpublished) study on the possibilities of harmonising the distribution grids so as to reduce, and even do away with, the major tariff disparities of the DSO in the Walloon Region.

2.3.3.3. Main activities of the CWaPE for the regional gas and electricity markets in 2007

As regards more specifically the regional gas and electricity markets, the main activities of the CWaPE in 2007 were focused on the following points:

- On green electricity:
 - Opinion concerning the offset between purchases and supplies to the end customer with a small capacity self-generating facility;
 - Opinion on amendments to decrees (decrees of 12 April 2001 and 19 December 2002);
 - Opinion on aid for generation;
 - Proposal on the procedures to be implemented in order to verify the renewables and/or CHP nature of the electricity supplied in the Walloon region;
 - Opinion concerning the reduction of additional quotas to companies in an industry-wide agreement;
 - Opinion on various measures to promote green electricity generated from new renewable sources of energy or co-generation;
 - Opinion concerning financial support for the generation of photovoltaic electricity;

- Report on the development of the green certificates market;
- In parallel to its role of adviser to the public authorities, the CWaPE is making an effort to inform small generators of green electricity by means of simplified notes.
- Opinion on the new appointment of gas and electricity distribution grid operators for municipalities where such appointments were limited in time;
- Opinion on the adaptation and expansion plans of grid operators;
- Opinions on applications by new suppliers;
- Examination of the reports of grid operators on the quality of their services in 2006;
- Analysis of the “confidentiality coordinators” reports;
- Proposal to amend the regulation applicable to licensing;
- Processing of applications for exemptions lodged for non-burial;
- Proposal and opinion on the revision of technical regulations in cooperation with the different market actors;
- Continuation of consultations to improve the methodology used to determine the cost-effectiveness of grid expansions;
- Monitoring of procedures for data interchange between actors;
- On energy tariff setting: making available a tariff simulator for residential customers, studies on price trends in the Walloon region, cooperation with the Competition Council;
- Membership and active participation in the Association of Issuing Bodies (AIB);
- Participation in a European study group on mixing options (or even replacement in certain grids) of biogas.

2.3.3.4. Implementation of the CWaPE’s power to impose penalties

In 2007, the CWaPE had on several occasions to serve formal notice to an actor to comply with the legislation. More rarely, the CWaPE had to impose a penalty (for instance, in the case of a grid operator who refused to supply protected customers). The CWaPE’s current power to impose penalties is relatively limited: the CWaPE may enjoin any natural or legal person to comply with the decrees organising the gas and electricity markets and their implementing instruments, within such a period as it specifies. If this person has not complied by the expiry of the stipulated time limit, the CWaPE may, having first heard or duly summonsed the party, impose an administrative fine of an amount that it will fix (subject, nonetheless, to maximum and minimum limits). If the person in question does not agree with the imposed fine, he may submit arguments to the contrary within 10

days of the notification served. After this time limit, the decision of the CWaPE becomes definitive. The procedure for imposing fines by the CWaPE will be amended in 2008 when the gas and electricity decrees are adapted.

2.3.3.5. Current and prospective projects

The problem of data communication between market actors continued to receive increasing attention in 2007. The CWaPE decided to allocate new resources to that end, in particular to monitor the production of a new manual undertaken by the multi-regional platform UMI, which is to be implemented in 2009.

In parallel, the discussion on a possible development of market models has continued and should produce results in 2008.

New prospects should emerge in 2008 through new Walloon decrees on the organisation of the gas and electricity markets.

2.3.4. BRUGEL (Commission for Electricity and Gas Regulation for the Brussels-Capital Region)

Operating year 2007 is a year of transition for the Brussels-Capital Region.

Until the Management Board of the Commission for Energy Regulation was appointed in September, the Government of the Brussels-Capital Region and its administration had assumed the role of regulator. Once appointed, the Management Board initially worked on a proposal for internal rules and procedures, on a proposal for the assignment of missions to policy officers and on such job descriptions as it deemed appropriate for the policy officers. It also issued opinions to the Government.

The main activities of the regional regulator in 2007 for the regional electricity market focused on the following points:

- New regulation ordinance enacted on 14 December 2006 by the Government of the Brussels-Capital Region;
- Monitoring of the total opening of the market (which took place on 1 January 2007); communication campaign (publication of brochures, etc.), making available of tools (website,

tariff comparator, etc.);

- Monitoring of market operators: opinions on supply licences, opinions concerning the investment plans of grid operators, opinions concerning the programme for carrying out the public service obligations of the distribution system operator;
- Policy to promote green and alternative electricity: certification of facilities, issuance of green certificates and quota control of green certificates to be submitted by electric power suppliers;